For use at 2:00 p.m., E.S.T.
Wednesday
March 17, 1999

Summary of Commentary on

Current Economic Conditions

by Federal Reserve District

March 1999

SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS BY FEDERAL RESERVE DISTRICTS

MARCH 1999

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SUMMARY[1]

The districts reported some further gains in economic activity in January and February, despite weakness in agriculture and a few manufacturing industries. Consumer spending continued to display strength, aided by post-holiday price discounting and mild weather in some regions. Motor vehicle sales increased, led by light trucks, and furniture sales benefited from robust home sales. Manufacturing activity expanded in most districts, although foreign competition and low energy prices depressed textile, apparel, and energy-related industries. Commercial real estate and construction activity, already at a high level, grew at a brisk pace in most districts. Residential construction was strong in most regions. Several districts reported a pickup in business lending, and a few noted that lenders' standards were stable to slightly tighter. Agriculture continued to be plagued by low farm commodity prices, and an increasing number of farmers were under financial stress. Labor markets remained tight. Finding qualified workers has become more difficult in several districts, and reports of faster wage increases were more widespread than in recent months. Prices of most goods remained little changed, and several districts said that businesses remain reluctant to press for price increases.

Consumer Spending: Retail sales remained strong in the first two months of the year, and most districts reported that activity was substantially higher than a year ago. Inventories were balanced and in line with future sales expectations. Boston, New York, Cleveland, Chicago, and Dallas experienced faster-than-expected sales growth, while in Atlanta, sales were flat or up only slightly from the prior year. In the Philadelphia, Richmond, Chicago, Kansas City, and San Francisco districts, substantial post-holiday price discounting helped move winter merchandise and boost sales, while Cleveland reported strong sales despite unusually small discounts. Healthy housing markets supported strong demand for furniture and home products in Boston, Cleveland, Richmond, Atlanta, Chicago, and Dallas. Apparel sales were lackluster in New York and Richmond but remained strong in Boston, Atlanta, and Chicago.

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[1] Prepared at the Federal Reserve Bank of Richmond and based on information collected before March 8, 1999. This document summarizes comments received from business and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

Automobile sales increased in many districts in January and February. Philadelphia, Cleveland, Chicago, Dallas, and San Francisco noted that motor vehicle sales--especially of sport-utility vehicles and light trucks--strengthened compared to December. Auto sales were lagging in Kansas City and flat in Minneapolis.

Two districts had upbeat reports on tourism. Resort activity was up from a year ago in the Atlanta District, while in Minneapolis skiing revenues were strong. In the Richmond District, mild weather damped revenues at ski areas but helped tourism in coastal regions. New York noted that their tourism boom had leveled off and that hotel occupancy rates had fallen.

Manufacturing: The tone of manufacturing improved in most districts, although some industries continued to be hampered by foreign competition. Growth in overall manufacturing activity strengthened in the New York, Philadelphia, Richmond, St. Louis, Minneapolis, and San Francisco districts. In the Boston, Cleveland, Atlanta, Chicago, and Dallas districts, manufacturing was described as mixed, while Kansas City said that its manufacturing sector remained weak.

Motor vehicle production moved higher in the Boston, Cleveland, Chicago, and San Francisco districts. In Cleveland and Chicago, heavy truck orders exceeded analysts' expectations in February and led some to raise their sales forecasts for 1999. The Boston and Richmond districts noted strength in the furniture industry, while St. Louis characterized its furniture industry as mixed. Several districts noted that shipments of semiconductors and high-tech equipment increased. Expectations for business conditions in coming months were mostly positive. Boston, for example, reported that most manufacturers' expectations were positive but cautious for 1999. Producers in the Philadelphia and Richmond districts expected orders and output to increase over the next six months.

Construction and Real Estate: Residential real estate activity remained vigorous in nearly all districts. Increases in housing starts were reported in the New York, Cleveland, Chicago, St. Louis, Minneapolis, and San Francisco districts. Residential construction was particularly active in Ohio, where some of the activity was described as speculative. Also, residential construction was said to be running at a record pace in St. Louis, and in the Minneapolis District, reports of increased residential construction were widespread. In contrast, new home construction eased a bit in the Atlanta, Dallas, and parts of the San Francisco District.

Contacts in the Chicago District indicated that existing home sales have slowed since December. Housing sales were described as brisk in the New York, Philadelphia, and Dallas districts. New home purchases were above the previous year's level in Kansas City and builders there were optimistic about the next few months. Home prices moved higher in the New York, Philadelphia, Cleveland, Richmond, and St. Louis districts.

In the Cleveland, Richmond, Minneapolis, and Kansas City districts, construction costs increased in recent weeks. Drywall and insulation shortages, as well as tight markets for skilled labor, placed upward pressure on prices. In contrast, San Francisco reported that lower labor costs in Utah and sluggish activity in Oregon had slowed construction cost increases in those areas.

Commercial real estate activity remained strong in most districts, although there were a few reports of slowing activity. Competition for commercial space intensified in the Carolinas. Rental rates rose in the New York and Philadelphia districts, and reached record high levels in the San Francisco Bay area. Chicago and Minneapolis noted faster growth in construction activity, particularly of public works projects. Boston reported an uptick in activity around Hartford, Connecticut, with several new construction projects planned. In contrast, Atlanta, Dallas, and San Francisco reported slowdowns in new construction, while activity in the Cleveland District was described as flat. Office leasing was said to be leveling off in Boston, and in the St. Louis District vacancy rates rose in central business districts.

Banking and Finance: Lenders were upbeat in most districts. Atlanta and San Francisco reported that overall demand for loans remained strong, and New York and Kansas City said that loans or loan demand picked up in recent weeks. Several districts noted strength in specific categories of lending: Chicago cited strong demand for consumer and business loans, while Dallas said that auto lending and home equity refinancing showed "signs of strength." Overall loan volumes were steady in Philadelphia and Richmond. Higher mortgage rates slowed the pace of lending in Richmond and caused a drop in loan originations and refinancing applications for some banks in the Chicago District. The only district reporting a decline in overall lending was St. Louis, where total loans at a group of large banks was said to be down 2.5 percent since the beginning of the year.

Reports on credit quality and delinquency rates were mixed. Chicago said that credit quality improved and New York reported lower delinquency rates for all types of loans. Cleveland, however, noted that many banks reported higher delinquency rates. In addition, automobile dealers in the Cleveland District expressed concerns about the credit worthiness of some new car buyers. San Francisco said that the only report of deteriorating credit quality was from the Oregon coast, where loan delinquencies rose.

Labor Markets, Wages, and Prices: Labor markets remained taut with higher employment levels reported in nearly all districts. Employers in the Chicago, Minneapolis, Kansas City, and Dallas districts continued to experience difficulty finding qualified workers. Markets for retail labor remained tight across much of the nation, especially in the New York and Kansas City districts, where finding even entry-level workers was said to be difficult. Cleveland also said that retail labor conditions remained tight, but somewhat less so than in December. Retailers in the Richmond District trimmed workers in an effort to control costs.

Temporary employment firms faced strong demand for their services in January and February. Boston and Chicago indicated that more businesses had recently turned to temporary employment firms to find workers. Cleveland and Richmond reported that temporary help firms were unable to meet their clients' demand for workers, raising the probability of future wage increases. The demand for contingent workers was mixed in the Dallas District, where requests from telecommunications firms, call centers, and banks remained at high levels, although demand from manufacturing and oil companies slackened.

Manufacturing employment was mixed across districts in January and February. St. Louis manufacturers increased their workforces, and plants in the Philadelphia District planned to add workers and lengthen the workweek in coming months. Boston and Richmond reported steady manufacturing employment, while declines were cited by New York, Cleveland, Kansas City, Dallas, and San Francisco.

The Boston, Cleveland, Richmond, Chicago, Minneapolis, Kansas City, and Dallas districts reported greater upward wage pressures in January and February. Generally stable wages were reported by New York, Atlanta, and San Francisco. Most districts indicated that higher wage costs were absorbed by businesses.

Low commodity prices and a perceived lack of pricing power by firms helped keep prices stable during January and February. Boston, Philadelphia, Richmond, Atlanta, Chicago, Minneapolis, Kansas City, and San Francisco reported generally steady prices, while Dallas indicated that price declines outnumbered price increases in that district. Rising lumber and drywall prices were reported by Cleveland and Minneapolis, while insulation and sheetrock prices inched up in the Kansas City District. Escalating health care costs continued to plague employers in the Atlanta, Minneapolis, and San Francisco districts.

Agriculture and Natural Resources: The weather had mixed impacts on agricultural production across the districts, and low commodity prices affected both agricultural and energy producers. Respondents from Richmond and Minneapolis said that above-normal temperatures generally improved crop and pasture conditions and reduced the need for supplemental feeding of livestock in some areas. Richmond and Kansas City noted, however, that warm weather had accelerated crop development, which increased the potential for frost damage. San Francisco reported "severe damage" to its citrus crop from a late December freeze. Agricultural banks in several districts stated that weak commodity prices had caused financial hardship for some farmers. Lenders in the Chicago District experienced a drop off in agricultural loan repayment rates compared to a year ago, and some hog farmers in the Kansas City District liquidated herds earlier than normal. Both districts noted that credit standards for agricultural loans had recently been raised. Contacts in the Dallas District said that a greater number of producers had left the farming business recently. In the energy sector, Minneapolis, Kansas City, and San Francisco reported that falling oil prices were causing some oil and gas wells to be withdrawn from production.

FIRST DISTRICT-BOSTON

Economic activity continues to expand in the First District. Retailers see ongoing strong consumer demand, while manufacturing results are mixed. For the most part, prices are said to be steady and wages growing moderately.

Retail

Contacts in the retail sector report continued expansion during the first two months of 1999 and news reports in early March cite unexpectedly strong sales growth for regional retailers. Sectors of strength include apparel, home furnishings, appliances, and discount retailers.

Employment is said to be holding steady on a same-store basis, increasing only with store expansions. Wage growth is reported to be in the same 4 to 6 percent range that characterized most of 1998. Most respondents say that prices continue to hold steady, primarily because of competitive pressures. Supplier prices are reported to be level, except for imported goods, for which prices are falling on account of the Asian slump, and lumber prices, which are said to have increased dramatically because of very strong U.S. residential construction activity. Gross margins are unchanged. Contacts say that moderate increases in operations are planned for 1999, with heavy investments being made in information technology. Looking forward, respondents express optimism about the economic outlook for the rest of 1999, but do not expect consumer spending to continue growing at its current pace.

Manufacturing

First District manufacturing contacts are about equally split as to whether recent business is up, down, or flat relative to a year ago. Companies selling to the automotive, furniture, and health care industries report positive trends, and demand for office supplies continues to rise. Sales of commercial aircraft parts are said to be increasing, although incoming orders suggest a sluggish period ahead. Sales of electronics, industrial machinery, and sports equipment are reported to be down. New England's paper and textile industries are being hurt by import competition, although some niches are now showing positive trends. Overall, exports to Asia continue to fall, with a couple of large manufacturers noting recent sales declines in China.

Manufacturers indicate that materials costs continue to be flat or down. The majority report steady selling prices. One-quarter report some small increases, partly reflecting a pass-through of higher labor costs. Apparel textile makers indicate somewhat lower selling prices, and some equipment manufacturers say customers are pressuring them for reductions.

Most contacts report little change in the size of their domestic workforce compared to either a year ago or a few months ago. However, several companies have laid off some production workers. Most new hiring is concentrated on sales, marketing, and service positions. Manufacturers mostly report that overall pay is increasing 3 to 5 percent, which some contacts note provides workers comfortable increases in real compensation. In general, wage pressures do not seem to be on the rise, although information technology personnel continue to command large increases.

Over half the contacts plan higher capital spending this year. The increases are primarily to introduce new technologies for production, product design, distribution, or information processing. Several firms also intend to expand overall capacity.

Most manufacturers have positive expectations for 1999. However, some mention the need to remain cautious or flexible in light of economic uncertainties.

Temporary Services

First District temporary employment firms report that 1999 is off to a reasonably good start as their business continues to expand. Demand continues to be strong, with firms reporting significant increases in their number of workers on assignment despite extremely tight labor markets across all industries. Wage inflation seems stable for most industries. For high tech workers, however, who are in extremely short supply (especially in the Boston area), robust wage growth continues. Prices that temp agencies charge firms for high tech workers are not rising as quickly as their wages because of increased competition; as a result, profit margins are being slightly squeezed. Revenues continue to rise due to increased business volume. Outside of high tech, clients have become more willing to accept higher prices. Most contacts foresee strong future growth for the staffing industry though some warn that "gravity has to work sometime."

Commercial Real Estate

After a long period of declining vacancy rates and increasing rental rates, the Boston office market seems to be leveling off a bit. While demand is still high, new construction of office buildings is increasing the supply of office space. So far there has been no decrease in rental rates, but contacts worry about overbuilding, especially since some of the new construction projects are speculative.

Hartford is said to be undergoing a "renaissance," caused in part by the upcoming construction of the Patriots' football stadium. Office and industrial vacancy rates have declined in Hartford, and several new construction projects are planned. Rhode Island, Maine, and Vermont contacts describe their commercial markets as "flat" and "steady." Outside a few pockets of increased rental activity, the markets in those states have been stable. Most contacts anticipate market conditions to remain unchanged during the next few months.

Nonbank Financial Services - Insurance

The majority of respondents at insurance companies experienced reductions in employment in the fourth quarter of 1998 and the first two months of 1999. The decline is attributed mostly to mergers and acquisitions. Respondents expect the downward trend in employment to continue for the rest of this year. Revenues were flat or down for the majority of respondents in the fourth quarter of 1998 compared to the fourth quarter of 1997. However, one property-casualty insurer reports dramatic increases in revenue, due to acquisitions.

SECOND DISTRICT--NEW YORK

The District's economy continues to grow at a brisk pace with only scattered signs of price pressures. Retailers report that sales were above plan in both January and February, with somewhat less discounting than last year on winter clearance merchandise; inventories were said to be satisfactory, albeit on the low side. The housing market has retained strong upward momentum in early 1999, with noteworthy improvement in upstate New York. After slowing in the fourth quarter, Manhattan office rents resumed their 15-20 percent rate of increase in January, as vacancy rates fell to cyclical lows.

Regional purchasing managers report a rebound in manufacturing activity in February, along with steady to declining commodity prices but a re-emergence of sharp upward price pressures for contracted services. Final costs of most goods and services remain stable, though there are scattered reports of hikes in restaurant prices and movie admissions. New York State payroll employment levels for both 1997 and 1998 were boosted considerably after recent benchmark revisions. Local banks report continued strong loan demand, leveling off in credit standards, and further declines in delinquency rates.

Consumer Spending

Retailers report that sales were generally above plan in both January and February. Most contacts report strong demand at clearance sales in January and brisk sales of spring merchandise in February, helped by mild weather. Among retailers, discounters continued to register the strongest sales gains compared to a year earlier, ranging from 4 to 9 percent, on a same-store basis; general merchandise chains reported more modest gains. Most sales categories performed well, though some contacts note lagging sales of toys, athletic footwear and accessories, and electronics. Inventories are mostly reported to be in good shape—none of the contacts indicate that they are too high, but one large chain says that inventories are too lean in certain categories. All of the retailers surveyed indicate that they and their major vendors are Y2K-compliant, and say they have no plans to accumulate extra inventories later this year.

Most retailers indicate steady wages, though one large chain reports that it is going to "bite the bullet and raise pay scales" this year, largely in response to rising turnover. Retailers indicate that prices of most goods are flat to somewhat lower; although ticket prices for apparel are lower than a year ago, some contacts note less aggressive markdowns than last year, thanks to strong demand at clearance sales. While prices of most goods and services remain stable, there are scattered reports of increases in restaurant and movie prices this winter in and around New York City.

Construction & Real Estate

The District's housing market showed further signs of strength in recent weeks. Single-family housing permits marginally exceeded last January's exceptional pace (despite snowstorms in western New York), while multi-family permits—mainly in New York City—were up 30 percent from a year ago; both segments were also strong in December. More currently, homebuilders in New Jersey report persistently heavy buyer traffic and sales in February and early March. Builders in New York State say that the market is strong and improving; even most parts of chronically sluggish upstate New York have improved substantially —notably the Rochester and Albany areas.

Remodeling contractors in both New York and New Jersey say they "have more jobs available than they can possibly do." Remodelers in Long Island and northern New Jersey report "numerous jobs in the six-figures." One New Jersey realtor described current market strength as "amazing." Similarly, New York State's market for existing single-family homes continued to be brisk in December and January, with sales up 8 percent from a year ago, led by the Syracuse, Rochester and Albany areas. Statewide, home prices were up more than 7 percent from a year earlier in January.

New York City's office market regained momentum in January, after slowing in the fourth quarter. In Manhattan, office availability rates fell to cyclical lows in January, while office rents resumed a steep uptrend. In the suburbs of Albany and Rochester, office vacancy rates fell to all-time lows of 2-3 percent in late 1998, while rates in suburban Syracuse and Buffalo were about double that; rates in the central business districts, however, continued to be a good deal higher.

Other Business Activity

Benchmark revisions to state payroll employment produced little change in New Jersey, but boosted New York State employment levels by roughly 1 percent in both 1997 and 1998. About half of the upward revision was in government (which had reportedly been undercounted going back to 1993); the other half mainly accrued to finance, construction and various services.

Regional purchasing managers surveys indicate a strong rebound in manufacturing in February, following a January slump. New York City area purchasers report that manufacturing improved sharply in February; they also note continued strength in nonmanufacturing activity. While prices paid for goods were flat to slightly lower, significant price pressures for contracted services re-emerged in February, led by computer and architectural services. Buffalo purchasing managers report a modest pickup in local manufacturing in February, with improvement in new orders and production but continued declines in employment; commodity prices were reported to be down noticeably in February.

New York City's tourism boom appears to have leveled off—hotel occupancy rates were somewhat lower than a year ago in January, while daily room rates registered a larger-than-normal seasonal decline and were up just 5 percent from a year ago. Albany-area hotels registered an increase in occupancy rates over the past year, despite a substantial expansion in the number of hotel rooms. Over the past year, there has been a sizable decline reported in the number of Canadians making day trips to the western New York State and an increase in New Yorkers visiting Ontario.

Financial Developments

According to a survey of senior loan officers at small- and medium-sized banks in the Second District, overall loan demand has increased in the past two months—particularly for residential and nonresidential mortgages, as well as for commercial and industrial loans. Refinancing activity turned down over the past two months. Bankers appeared more willing to lend than they were two months ago, and credit standards, which had been tightened through most of 1998, remained stable.

Interest rates on residential and nonresidential mortgages remained unchanged since the last survey, while consumer and commercial loan rates fell. Average deposit interest rates decreased over the past two months, as over half of the bankers surveyed reported lower deposit rates. Delinquency rates decreased for all types of loans, indicating continued improvement in the quality of credit.

THIRD DISTRICT - PHILADELPHIA

Business conditions in the Third District generally improved during February. Manufacturing shipments and orders increased. Retail sales exceeded year-ago and prior month results. Auto sales have also increased. Bank real estate lending moved up slightly, but business and consumer lending has been steady. Sales of both new and existing homes have been rising strongly. Commercial real estate vacancies have been falling and rents have been rising.

Third District business contacts have positive outlooks. Manufacturers expect demand for their products to continue on an upward trend, and they plan to increase employment. Retailers anticipate further growth in sales as the spring season gets under way. Auto dealers expect sales to remain healthy. Home builders forecast construction at or above the current pace into the summer, and real estate agents expect sales of existing homes to remain strong. Commercial real estate contacts anticipate a balanced market and a steady pace of construction for the rest of the year.

MANUFACTURING

Third District manufacturing activity increased in February, according to industrial firms in the region. One-third of the companies contacted said shipments and orders during February exceeded January levels, although about half said business was steady. Increases were reported from most major industrial sectors in the District. Producers of lumber and machinery had relatively strong gains; in contrast, makers of food products and textiles indicated that demand for their products had slipped. Overall, order backlogs at area plants remained steady in February and inventories edged down; however, some firms in textile industries indicated that inventories were too high relative to sales.

Manufacturers in the District generally expect business to increase during the next six months. They forecast increases in orders and output, and they plan to add workers and lengthen the workweek. On balance, area manufacturers expect prices of both inputs and products sold to rise only modestly.

RETAIL

Retailers in the region indicated that sales increased by a substantial amount in February from January and from a year ago. Several merchants noted that a significant portion of February sales was attributable to clearance of winter merchandise at substantially discounted prices. Nonetheless, store executives said sales of spring goods, especially women's and children's apparel, were healthy. If the current trend continues, merchants expect sales in March of this year to exceed sales in March of last year. Store officials generally described inventories as satisfactory, as reduced prices have helped clear out winter goods and consumers have started buying spring merchandise.

Sales of new motor vehicles have been on the rise. Dealers reported that manufacturers' shipments of popular models have increased recently, facilitating a better sales rate with less use of incentives. Dealers expect sales to remain at a strong pace, even if there is some slippage from the current rate.

FINANCE

Most of the bankers contacted for this report said loan volume was steady during February. Although a few indicated that they were increasing business loans slightly, mainly to firms that were purchasing equipment or expanding facilities, most bank lending officers described commercial and industrial loan demand as flat. Bankers also said there has been virtually no growth in consumer lending. Real estate lending activity has been high in the region, but net growth in real estate loans outstanding has been slight. Much of the new mortgage loans booked replace mortgages paid off, and refinancings do not boost total real estate credit outstanding.

REAL ESTATE AND CONSTRUCTION

Commercial real estate markets remain healthy, according to recent reports from brokers and property managers. The estimated vacancy rate for the central business district of Philadelphia was 14 percent, unchanged from the fall of last year. Vacancy rates in suburban markets have been declining and are currently estimated in a range of 6 to 12 percent, depending on location. Rents have risen up to 10 percent from a year ago in both the suburbs and the central business district. Demand for industrial space remains strong, but a steady supply of new buildings has kept vacancy rates steady. Rental rates, however, have moved up, reflecting an increasing need for more technologically advanced buildings. Commercial real estate contacts forecast continued construction of build-to-suit office and industrial buildings in markets outside central Philadelphia and some limited speculative construction in a few areas. They expect supply and demand to remain nearly in balance through 1999.

Home builders and residential real estate agents reported a very brisk sales pace in February. Brokers estimate price appreciation of existing homes at around 3 percent over the past 12 months for most parts of the region, but gains have been higher in a few places. Mild weather accounts for some of the strength in February sales, according to builders and real estate agents, but they also cite buoyant consumer confidence and healthy personal income in the region as factors that should underpin a continuing high rate of sales.

FOURTH DISTRICT - CLEVELAND

General Business Conditions

The Fourth District's economy is still growing, although somewhat unevenly by industry. Labor markets remain tight and reports of wage increases are growing. Indeed, the rate of joblessness in some areas has descended to levels previously unseen (about 2% in the Cincinnati/Northern Kentucky region.)

The District's temporary employment agencies were unable to keep pace with demand in February, and all of the agencies surveyed indicate having increased wages since the beginning of the year for a wide range of workers. Several agencies are preparing for another round of wage increases within the next few months.

General laborers are in short supply in the southern parts of the District, even in the manufacturing sector where labor markets have been softer. Elsewhere, firms continue to report a shortage of administrative support, including experienced secretaries.

District transporters report a leveling off in shipping activity this year, and business is modestly below levels of a year ago. International traffic has improved, as both imports and exports have grown since the last report. Imports remain especially strong, however, and the imbalance between imports and exports persists. Shippers are expected to hike rates on Asian routes to compensate for capacity excesses on return trips.

Agricultural commodity prices, which have stabilized recently, are substantially below levels of a year ago, although dairy prices remain elevated. In Pennsylvania reduced soil moisture has become a source of concern, and Kentucky tobacco farmers report reduced crop quotas for 1999.

Construction

Residential building has picked up from the brisk pace of 1998. Residential building activity in central Ohio is especially strong. The volume of commercial construction does not appear as universally strong as residential construction, though none of the sources we contacted indicate any drop in activity from earlier in the year.

Shortages in particular trades continue and are adding to wage pressures in those areas. Lumber and drywall are in short supply and costs are rising. Still, some builders report that profit margins have improved from last year.

Reports of speculative building remain spotty by region and category. Land speculation in northeast Ohio is noted by a few sources, and a few commercial contacts also indicate that speculative building and development has increased.

Industrial Activity

District manufacturing is holding steady or showing modest gains. Export markets have stabilized and show modest improvement in some cases. In the steel industry, strong domestic orders have eased competitive pressures created by foreign imports. Capital goods makers note renewed broad-based growth in orders and production after a mixed fourth-quarter performance.

Semiconductors, agricultural machinery, and construction equipment have all picked up following relatively soft year-end numbers. Transportation equipment makers are posting gains from an already high level of production. Heavy truck orders rebounded in February, and the orders backlog in this industry extends almost through the end of the year. One industry source expects production in 1999 to top last year's record level.

Industrial commodity prices are either flat or falling across a range of goods. Although employment is rising again and wage growth has picked up for some workers, industrial producers see productivity gains neutralizing employment cost pressures.

Consumer Spending

The majority of retailers report strong, better-than-expected sales in the first two months of the year. Seasonal discounts are reported less than usual due to a strong consumer appetite. Inventory levels are good and spring merchandise is already in stock. Furniture stores report very strong sales, with inventories and prices adequate. Retailers maintain that the labor market is still tight, but less so than in December.

Auto sales in February were good or better. Manufacturer incentives, combined with a strong economy have kept the industry active in a typically slow season. New vehicle inventories are in line with sales expectations, with fewer-than-normal shortages reported. Even the previously soft used-car market has seen good sales recently.

Banking and Finance

Lending activity in the District is good for both commercial and consumer loans, although the growth rate of commercial loans has slowed. Small business borrowing is mixed by institution, and some businesses are finding credit more difficult to obtain. The spread between borrowing and lending rates is still shrinking.

An increase in the loan delinquency rate is reported by many, if not most, banks. District auto dealers expressed concern about an apparent deterioration in the creditworthiness of some new car buyers. One source noted a rise in auto repossessions in the past year.

FIFTH DISTRICT – RICHMOND

Overview: Fifth District economic activity continued to advance at a healthy pace during the past two months. Retailers reported robust sales and brisk shopper traffic but services providers gave mixed reports. In manufacturing, shipments rose modestly and producers expressed more optimism regarding future business prospects. Real estate activity in the District continued upbeat, despite a somewhat slower pace of expansion in commercial activity in some areas. Loan demand remained generally strong across the District. Mild weather in January and February helped District crops and boosted tourist activity at coastal resorts but reduced patronage at ski resorts. Labor markets tightened, although wage increases remained moderate. Prices changed little in manufacturing and rose only slightly in the services sector.

Retail: Warm weather and unusually large post-holiday price discounts sparked a sharp rise in retail sales in recent weeks. Shopper traffic was particularly brisk in February and sales of big-ticket items picked up. Furniture sales were notably strong, benefiting from a robust housing market. One Northern Virginia furniture retailer commented that "almost all of our sales have been to people who just closed on a new house." Sales of winter apparel, however, remained lackluster. A department store manager in Charleston, W.V., complained that it had been "too warm; we weren't able to sell winter goods at any price!" Inventories rose as apparel retailers ordered larger-than-normal shipments of spring lines, signaling their optimism regarding sales in upcoming months. Despite their expectations of strong demand, retailers continued to say that they had no pricing power; many reported trimming workforces in an effort to control costs and hold the line on prices.

Services: Services sector activity has been mixed across industries since the beginning of the year. Electric and gas utilities reported declining revenues because of unseasonably mild weather. Business services and hotels, however, enjoyed substantial revenue growth. A hotelier in Baltimore, Md., attributed higher revenues to increased automobile and air travel. Employment in the services sector fell in recent weeks and wage pressures declined, but prices were little changed. Services providers remained optimistic about the demand for their services in coming months.

Manufacturing: District manufacturing activity strengthened since our last report. New orders and order backlogs grew more quickly in February and capacity utilization rates rose for the first time since October. Manufacturers reported increased shipments, particularly of lumber, furniture, paper, and food. A North Carolina furniture producer told us that he expected strong furniture sales to continue this year because housing starts remained buoyant and unemployment remained low. Manufacturing employment in the District was little changed in January and February despite increased layoffs in the textile industry. Producers reported a pickup in wage growth, but indicated that their prices remained flat. Looking forward, most manufacturers were more optimistic regarding the growth of shipments and new orders during the next six months.

Finance: District loan officers reported generally steady lending activity since our last Beige Book. Solid growth in business activity generated brisk demand for commercial loans. Commercial lending remained competitive; a banker in Virginia said that he had to be "proactive" just to avoid losing his existing customers to an ever-growing number of rivals. Residential mortgage lending remained strong in January although the pace slackened somewhat in recent weeks as mortgage rates moved higher. A lender in Greenville, S.C., noted that higher mortgage rates made it more difficult for first-time homebuyers to qualify for loans. He speculated that further increases in mortgage rates could appreciably reduce loan demand.

Real Estate: Residential real estate activity expanded at a healthy clip in January and February. Realtors told us that homes in all price ranges were moving quickly and that a "seller's market" remained intact. Home sellers were said to be "getting their asking prices" in most areas, especially in Maryland, where multiple offers on properties were common. A realtor in Richmond, Va., remarked that the pace of house sales was "as fast as a race car." In some areas, strong demand for housing contributed to shortages of labor and building materials--particularly of drywall and insulation. Recent increases in mortgage rates have had both positive and negative impacts on residential real estate activity. A West Virginia realtor told us that some of her clients were getting nervous about rates going up and were trying to get in "under the wire," implying that higher rates may have stimulated activity there. On the other hand, a Charlotte, N.C., contact said that mortgage rate increases had caused "some weakness" in entry-level home sales in his area.

Commercial real estate activity also remained strong in recent weeks, although the pace of growth slowed somewhat outside of the Carolinas. A Washington, D.C., realtor said that people were simply "running out of steam" in his area. In contrast, activity in the Carolinas remained robust; one North Carolina agent likened the market there to a "runaway freight train." Competition for commercial space in the Carolinas has intensified in recent weeks. A Raleigh, N.C., realtor said that tenants were willing to pay additional "fees" in return for priority access to available retail space. According to a contact in Columbia, S.C., small tenants in that area were being "forced out of buildings" once their leases expired to make room for expansion by larger, more established tenants.

Tourism: Unseasonably mild weather in recent weeks had mixed impacts on District tourist activity. Tourism in coastal areas benefited; one hotelier on the Outer Banks of North Carolina, for example, reported that her resort was "booked to capacity" during Valentine's Day weekend. She also said several restaurants that normally close for the winter and reopen around Easter had opened early this year because of strong tourist traffic. Mild weather, however, contributed to lower revenues at several area ski resorts this winter. A contact at a Virginia resort that offers both ski and golf facilities noted that higher revenue from golfing had helped offset sharply lower revenues from skiing.

Temporary Employment: The demand for temporary workers picked up since our last report, exerting additional strains on the District's already taut labor markets. Most contacts at employment agencies told us that employers continued to complain about the shortage of workers, but so far, relatively few were offering substantially higher wages to attract employees. A greater number of agents, however, now say that they expect wages to rise at a quicker pace in coming months. A recruiter in Charlotte, N.C., remarked that employers will almost certainly need to raise wages if labor markets get any tighter. In his words, "the dam can only hold back the water for so much longer."

Agriculture: Above-normal temperatures generally benefited District farming activity. Warm weather helped small grain crops, which were reported to be unusually mature this year. Mild weather conditions also boosted winter pastures, reducing the demand for feed supplies by livestock producers. Due to the warmer weather, however, fruit trees in some areas showed signs of early budding, increasing the risk of spring frost damage to the District's peach and apple crops.

SIXTH DISTRICT – ATLANTA

Summary: The Southeast economy continued to post moderate growth into late winter, and contacts are mostly upbeat about the near-term outlook. Although merchants' reports on sales have been mixed, most expect improvement over the next few months. Prospects for the tourism and hospitality sector are positive, with continuing expansions of attractions and properties. Residential construction and sales weakened a little but remain at high levels. Commercial real estate markets are healthy but with some modest deceleration in new construction. Factory production has been sluggish in sectors primarily affected by foreign imports, but other sectors are adding to payrolls. Bankers report continuing strong loan demand. Tight labor markets are adversely impacting high-tech employers, but reports note mostly stable wage changes for other employers. Prices are expected to hold steady over the next few months, with a few exceptions.

Consumer Spending: Recent sales reports from District retailers during January and February were mixed. Most managers said that recent sales had generally met their expectations. The strongest sellers have been women's and children's apparel, cosmetics and home-related products, while men's apparel sales have been weak. Most contacts said that inventories were balanced overall. The majority of retailers anticipate that first quarter sales will be flat to slightly up compared with last year and second quarter sales will be slightly better.

Tourism and Business Travel: Reports from the tourism and hospitality sector remain positive. Bookings at a large resort in Miami are above those of a year ago, and spokesmen are upbeat about recent expansion plans. Miami tourism officials characterize occupancies and room rates as "very good." The south Florida cruise industry reportedly had its best year ever in 1998, and 1999 bookings are strong. Occupancy rates in metro Atlanta hotels improved in 1998, ending three years of declines. Hotel operators are optimistic and expect occupancy to continue to grow at a moderate rate in 1999. Mississippi's casinos had a record year in 1998 with revenue up 10 percent from 1997; their outlook remains positive based on early 1999 figures. The Beau Rivage casino in Biloxi is slated to open in mid-March and will employ 4,200 people.

Construction: Most District builders report that the pace of single-family home construction in January was up slightly compared with a year ago, and new home sales were generally flat. During February, they report new home construction and sales weakened somewhat on a year-over-year basis. According to District Realtors, home sales were flat to slightly up in both January and February. Inventories are generally balanced, although several builders in Florida and Georgia indicated there was a shortage of lots. Looking forward, the majority of builders expect home construction will be flat during the first and second quarters compared with last year, and Realtors anticipate home sales during the same period will approximate those of last year.

Contacts report that the pace of commercial construction in the District declined somewhat during late winter, but overall, office, industrial and retail markets in the region remain healthy. Office and industrial vacancy rates have risen somewhat in several key markets but the increase remains subdued.

Manufacturing: Factory activity has been mixed. The number of operating drilling rigs in Louisiana has reached new lows, and contacts report that layoffs in support industries are beginning to mount. Auto parts producers report sluggish orders. A manufacturer of auto components with plants in Mississippi and Louisiana is closing, displacing 635 workers. Foreign competition has resulted in new announcements of more layoffs in Georgia and Tennessee's apparel industry. More positively, some high-tech sectors continue to expand. New orders and the factory workweek are increasing for District producers of electrical and electronic equipment. A large domestic order for set top boxes for cable television has helped to offset slumping overseas sales for a Georgia company. Plans have recently been announced for two new computer plants in Mississippi. The continued boom in high-speed telecommunications is resulting in plant expansions around the District.

Financial: Bankers report that overall loan demand and lending remain strong throughout the Southeast. Consumer loan volume has continued to expand. Commercial sector lending and demand for mortgage refinancing and purchases remain robust. There has been no systematic trend emerging from reports of increasing or decreasing credit quality standards across the District.

Wages and Prices: Although labor markets are tight throughout the District, wage pressures remain relatively stable, according to most contacts. Bonuses and incentive pay are cited as growing components of compensation. Despite this, per-unit labor costs basis are declining for some firms as a result of downsizing, reorganization, and outsourcing. Some companies are limiting wage increases of non-high-tech jobs in order to offset costs in the high demand occupations. A few job categories remain, such as those in information technology, where wages have been increasing. In some parts of the District, foreign immigration is helping to alleviate labor shortages. In Nashville, more companies are planning to cut payrolls this spring than in the recent past, indicating some easing of the labor shortage there. Prices are expected to hold steady over the next few months, according to most contacts. Health-care costs are expected to continue to rise. Prescription drug prices are escalating, and health maintenance organizations are increasing premiums.

SEVENTH DISTRICT -- CHICAGO

Summary. The Seventh District economy continued to expand modestly in early 1999, despite weakness in some of the region's mainstay industries. Consumer spending remained strong, exceeding many merchants' expectations. Home sales slowed somewhat from December's torrid pace, but overall construction activity remained brisk. Manufacturing activity was mixed as strength persisted in some key industry segments, such as motor vehicles, while softness continued in others, particularly steel and agricultural equipment. Lenders indicated that loan demand remained strong even as mortgage refinancing activity fell off somewhat. Worker shortages persisted in the District and there were a few new reports of increasing wages in entry-level positions. Low commodity prices and a poor farm income outlook helped push farmland values down in Illinois and Iowa during the last three months of 1998.

Consumer spending. Retail sales in January and February met or exceeded most contacts' expectations, led by strength in sales of home-related items and light vehicles. Exceptionally strong home sales in late 1998 continued to boost sales of big-ticket items, such as furniture and appliances, as well as home improvement goods, such as tools and paint. Strength in apparel sales was broad-based, although one contact indicated that discounting had been planned to generate sales instead of profits. Inventories were generally reported to be in line with sales expectations heading into the spring. Discounters, again, fared better than general merchandise stores. A contact at one national general merchandiser suggested that the increasingly price-driven retail industry was forcing the company to rethink its pricing strategy. District auto dealers reported that sales mirrored the strength in the nation, reflecting high consumer confidence and increased affordability. Despite strong consumer demand, price pressures at the retail level, for the most part, remained subdued.

Construction/real estate. Overall construction activity remained robust in the District even as December's hot housing market cooled off somewhat early in 1999. Existing home sales in the Midwest were down only slightly from December, according to a national report, but a leading real estate firm in one of the District's largest metro areas reported their second best January sales results ever, down less than 1 percent from last January's record level. Most homebuilders contacted noted that once seasonal factors are considered, the market for new homes appeared to be strong and steady. Builders of entry-level homes noted they were struggling with "razor" thin margins resulting from intense competition, leading to some consolidation in the industry. Commercial construction activity generally remained strong, but reports were mixed. Contacts in some metro areas reported a resurgence in downtown retail building activity, particularly in Milwaukee. On the other hand, another contact noted that some office projects already underway in downtown Chicago had been put on hold. Apartment vacancy rates remained very low and rents were reported to be up about 5 percent from a year ago in the Chicago area, where two new downtown high-rise apartment projects were announced in the last month. Activity on public projects and infrastructure remained strong in most areas and may have picked up in February, according to contacts.

Manufacturing. District manufacturing activity remained mixed in January and February, as some key industry segments continued to be adversely affected by economic turmoil abroad. Light vehicle production remained exceptionally strong in the region as manufacturers benefitted from February sales results that exceeded virtually all expectations. As a result, most auto analysts have already increased their sales forecasts for 1999. Despite strong sales, as well as lean inventories, most industry analysts expected auto prices to remain soft. Demand for heavy trucks also remained very strong, as low fuel prices have made truck transportation more competitive and profitable. Production of most construction-related equipment was "going gangbusters" according to contacts, but demand for other heavy equipment remained lackluster as a result of soft export markets and problems in the farm sector. Agricultural equipment continued to be the weakest performer in the heavy equipment sector, with industry analysts expecting sales losses to exceed 20 percent in 1999. Pricing for heavy equipment remained soft, even for most construction-related products that were selling well. The region's steel industry, while still struggling, showed some slight improvement early in 1999 as domestic consumption remained strong and imports fell off in December and January. Prices for some steel products increased modestly in February, but remained well below year ago levels.

Banking/finance. Contacts in the financial services industry indicated that demand for both consumer and business loans remained strong. Consumer lending activity generally remained brisk, although reports of mortgage lending became mixed. Bankers in some areas indicated that mortgage originations and refinancing applications peaked in the fourth quarter of 1998 and had fallen off somewhat early in 1999 as interest rates on fixed-rate mortgages trended up. One banker, however, suggested that rising interest rates hadn't necessarily dampened overall demand, but shifted it from fixed-rate to variable-rate or balloon mortgages. Credit quality continued to improve as consumers paid down their credit card debts with retailers, and used more cash and debit cards for purchases. Some analysts suggested that consumer credit quality typically improves with a surge in refinancing activity. Business lending activity generally remained strong as well. Competition for quality middle-market customers remained intense and continued to squeeze margins for most institutions. A few bankers reported that margins on syndicated loans had improved as a result of Japanese banks pulling out of the market. With few exceptions, the quality of commercial loan portfolios was reported to be good as borrowers remained diligent in containing costs and improving profits.

Labor markets. District labor markets remained much tighter than in the rest of the nation during January and February, and most contacts continued to report difficulties finding and retaining workers. The average unemployment rate for District states was 3.6 percent in January, down slightly from December, and well below the national average of 4.3 percent. There was no evidence suggesting that any slack developed in February and early March. Long-running shortages in information technology and skilled trade occupations persisted throughout most of the District. Contacts with casual dining establishments indicated that staffing problems were hampering expansion plans as well as hours of operation at some locations. Shortages of truck drivers were also noted by contacts, with one firm adding that they were continually upgrading trucks and equipment as part of the overall package to attract and retain drivers. An accounting firm in one large metro area reported difficulty in finding accounting professionals, and the firm was turning to more temporary help. Wage pressures continued in those occupations where severe shortages have persisted, but there were also new reports of wage increases for entry-level positions. Several contacts, citing significant resistance to price increases, insisted that increased wages would have to be offset by productivity gains or other cost-cutting measures.

Agriculture. A survey of agricultural bankers indicated that farmland values declined over the last three months of 1998 in Illinois and Iowa, but rose in Indiana, Michigan, and Wisconsin. The survey also showed that farm loan repayment rates were down from a year earlier due to low grain and livestock prices. The situation was relatively worse in Illinois, Indiana, and Iowa because of their greater dependence on hog, corn, and soybean enterprises. Bankers also noted that credit standards for agricultural loans had been raised. The impact of low commodity prices continued to haunt District farmers, as corn and soybean prices decreased through February while hog prices stabilized. Milk prices paid to farmers, which had increased throughout the second half of 1998, fell in January and February, but remained above a year earlier.

EIGHTH DISTRICT - ST. LOUIS

Summary

The District economy is still operating at a high level and growing moderately. Weakness in the agricultural sector is the only notable exception. The District's position as a distribution center continues to solidify, as UPS and FedEx attract more businesses to their hubs. District auto production is expected to increase because of a new line at a Ford plant. According to Manpower's second-quarter employment outlook survey, firms in the District's four major cities have upped their hiring expectations significantly from the previous survey. Most District metropolitan areas ended 1998 with more residential building permits issued than a year earlier; in several instances, it was a record year. Nonresidential real estate markets have been mixed. Total loans at large District banks have been down since the beginning of the year, with consumer loans seeing the biggest decline. Most major crop and livestock prices trended modestly lower since our last report.

Manufacturing and Other Business Activity

Most District contacts continue to see growth in sales and employment. Although reports of tight labor markets have tapered off somewhat, other market indicators suggest that, rather than there being a real change in market conditions, contacts have just stopped mentioning it. Energy producers and agricultural areas of the District, especially the southern states, have been hit extremely hard by falling prices.

The District continues to attract new businesses that see it as a distribution hub, especially in the Louisville and Memphis regions. The presence of UPS and FedEx and their geographic locations are most often cited as reasons for firms picking these areas. Several firms have announced that they have chosen the St. Louis region for their new service-response (calling) centers. The District furniture industry is seeing more mixed results recently. Larger, more efficient plants report continued strong sales, while smaller, less efficient plants are struggling due to cost disadvantages. District auto production will grow as Ford adds a line to produce its new sport-utility vehicle to the Louisville truck plant. Employment in St. Louis will receive a boost as Boeing consolidates its missile production there.

Several other reorganizations and consolidations, however, mean job losses. Declining domestic demand for cigarettes has led Philip Morris to announce it will close its Louisville plant. The ever-dwindling District apparel sector is seeing additional fallout: Levi Strauss is closing a plant because of slack demand for jeans, and a shirt manufacturer is shuttering its plant because of overseas competition. Some contacts mentioned a falloff in their exports because of the devaluation of the Brazilian *real*.

Employment Outlook

Current labor market conditions, while solid, are expected to improve further, according to Manpower's February employment outlook survey. Labor demand in the District's four major cities is expected to be even greater during the March-June 1999 period than was anticipated in the previous survey taken in November 1998. In particular, the current survey shows that, on net (percentage reporting increase less percentage reporting decrease), 24 percent of the surveyed firms in the District's major cities plan to increase employment. This is a sizable uptick from the 8 percent net reported in the November 1998 survey, but identical to the percentage noted in the February 1998 survey. Employment gains in the second quarter are expected to be strongest in Little Rock, Louisville and Memphis, with somewhat less strength evident in the St. Louis market.

Real Estate and Construction

By the end of 1998, ten of the District's 12 metropolitan areas had issued more residential construction permits than they had in 1997. In all, four metro areas had record years for total residential construction in 1998, and six metro areas had built more single-family homes than ever before. This pace seems to have continued into 1999. District real estate agents report continued strong sales (adjusted for the season) and moderate price gains. Nonresidential markets are more mixed. Several agents have noted a softening in the office market and mildly increasing vacancy rates in central business districts. Commercial and industrial markets, however, remain relatively strong in most parts of the District.

Banking and Finance

Total loans on the books of a sample of large District banks have declined 2.5 percent since the start of the year. All loan categories have dropped from their 1998 year-end levels, with consumer loans posting the sharpest decline at 2.4 percent, followed closely by real estate loans with a 2.1 percent decline. Commercial and industrial loans, however, are essentially unchanged, declining just 0.1 percent. One year ago, total loans at these banks increased 2.4 percent during the same period.

Agriculture and Natural Resources

Crop and livestock prices generally trended downward during the past month and a half, paced by a more than 14 percent decline in soybean prices. At the other end of the spectrum, cotton prices rallied a bit after falling to a five-year low in February, and feeder cattle prices continue to rally from their lows posted last September. Two major surveys of U.S. cotton farmers' 1999 planting intentions show a modest increase in acreage from a year earlier. In the mid-South region, however, a major trade organization expects cotton acreage to dip modestly this year. Indeed, reports from contacts in the southern part of the District suggest that some farmers plan to devote more acres to soybeans this year, a flexibility offered by the recent Freedom to Farm legislation.

NINTH DISTRICT--MINNEAPOLIS

In early 1999 the pace of Ninth District business activity has picked up from the strong conditions reported at the beginning of the year, although natural-resource based industries remain in the doldrums. Businesses and forecasters are more optimistic now than in December. The forward momentum continues for construction, consumer spending and manufacturing. Low commodity prices continue to depress farm income, curb iron mining and stall oil exploration. Businesses would like to hire additional workers and are raising wages to attract them. They, however, are reporting few other price increases.

Business Sentiment

"Nothing short of awesome," is the Minnesota state economist's current description of the national and state economies. Minnesota is now projecting a state budget surplus of $4.1 billion over the next three years, up from a $3.3 billion surplus that was projected in early December. A recent survey of Upper Midwest business supports his contention. In February 64 percent of respondents reported increasing sales as contrasted to 53 percent in December. Ninth District banks report strong loan demand.

Construction and Real Estate

“Home builders have greatest January in 7 years,” proclaims a Minneapolis news article. Housing permits increased all across the region in January from the previous year’s level. Other construction remains strong, with January contract awards in Minnesota and the Dakotas 15 percent over year-earlier levels. Medical and health care facility construction projects are under way in Minnesota and Montana, and a large factory hog farm is planned in South Dakota. Public works projects are increasing across the district, with highway construction driven higher in Minnesota, Montana and South Dakota.

Consumer Spending and Tourism

Retail spending showed continued momentum in early 1999. A major electronic goods retailer reports sales up substantially so far in 1999. A major Minneapolis/St. Paul retailer reports strong sales gains in February and is "cautiously optimistic" about future sales. Elsewhere, a mall manager in North Dakota reports sales up 5 percent from a year ago for the first seven weeks of 1999.

Vehicle registrations increased significantly in South Dakota for the month of January compared to a year earlier, but decreased slightly in North Dakota. A North Dakota auto dealer association spokesperson expects the trend in auto sales to be "flat at best," due to the lagging agriculture and oil sectors.

After a slow start in December, winter tourism picked up in January and February. In northern Minnesota a major ski hill recorded record weekends in January and February, following a weak December. In the Upper Peninsula of Michigan most motels were full on weekends in February, as contrasted to vacancies in December. South Dakota ski resorts also report a strong season, but a lack of snow has slowed snowmobiling. Meanwhile, in northern Montana business at a ski resort has been up only slightly from a year ago, due to the unfavorable exchange rate with Canada.

Manufacturing

District manufacturing remains quite robust, despite the restraining influence of a weak international economy. A computer-components manufacturer recently announced a major expansion in western Wisconsin, which could add more than 1,000 jobs. A construction equipment manufacturer intends to expand its two North Dakota manufacturing plants, and a window manufacturer is adding workers at its North Dakota plant. High-tech manufacturing is bolstering production in South Dakota, according to a regional survey of purchasing managers. Moreover, several small manufacturers report strong, improving sales, according to a recent survey of Upper Midwest business.

Weak foreign economies, however, continue to constrain manufacturing. The Asian economic collapse has weakened demand for paper, and a major paper manufacturer recently announced the closing of a plant in northwestern Minnesota. Moreover, two western Wisconsin manufacturers attribute soft sales to weak international business, and according to a regional survey of purchasing managers, Minnesota manufacturers tied to international markets, especially high tech, continue to report problems.

Energy and Mining

Mineral-based industries remain in the doldrums. In response to weakening demand for domestic steel, one Minnesota mine shut down a taconite pellet line last fall, and it is uncertain whether the line will restart this spring as hoped, states a company spokesperson. Another Minnesota taconite producer is expected to lay off at least 100 workers by late May and could cut production this year by 18 percent. Meanwhile, "oil exploration is at a standstill," reports a bank director. No rigs are currently working in North Dakota and only five in Montana as compared to 16 and 9, respectively, a year ago.

Agriculture

Like mining, agriculture remains stalled. Corn, soybean and wheat prices continue to remain near historic lows. Moreover, milk prices are declining, due to increased production. Hog prices have recently increased from December's extremely low prices but still remain below the break-even point for many producers. Several outbreaks of hog pseudorabies have been reported due to cash-strapped hog farmers eliminating vaccinations. The mild winter weather and low feed prices, however, have benefited cattle, dairy and hog producers.

"The low commodity and livestock prices are drastically taking their toll on the net worth/capital of the farmers and drastically diminishing their ability to repay loans," reports a local agriculture lender. Based on preliminary results of the Ninth District's first quarter survey of agricultural credit conditions, 61 percent of respondents reported a below normal rate of loan repayment compared to 51 percent of the fourth quarter survey respondents. In both the first quarter 1999 survey and the fourth quarter 1998 survey approximately 70 percent of respondents reported farm income decreases from the previous year's levels.

Employment, Wages and Prices

"Most firms would hire qualified workers if they could find them," a recent survey of Upper Midwest businesses reports. But it is tough; unemployment rates are under 3 percent in nine out of the district's 14 metropolitan statistical areas (MSAs). Nevertheless, 60 percent of the St. Paul firms responding to a staffing firm's recent survey indicated they plan to add workers in the second quarter, which is up from the 46 percent giving that response a year ago.

In addition to innovative incentives and recruiting schemes to attract workers, employers are raising wages. A telemarketing firm recently boosted its starting wage to $7.50 an hour from $6.75. Plus, several large district firms indicated that they are increasing wages 4 percent to 5 percent this year. Increasing health insurance premiums are pushing up compensation costs, states a Minnesota union official.

While firms have to raise wages, they "can't increase prices," says a Minneapolis/St. Paul banker. Competitive pressures are keeping firms from raising prices, but low import prices are helping many of them to keep their costs down. Seventy percent of participants to a survey of Upper Midwest business reported stable or declining prices for their products, the same percentage as in December. Construction input prices, however, have been rising, due to the strong pace of building activity.

TENTH DISTRICT - KANSAS CITY

Overview. The district economy continued to grow moderately last month. Retail sales again posted solid gains, and manufacturing registered its first improvement in months. Construction activity eased slightly due to colder weather but remained well above last year's pace. Energy activity declined as prices took another turn for the worse. In the farm economy, the winter wheat crop was in good condition, but hog farmers continued to suffer from low prices. Labor markets remained very tight in most of the district, with wage pressures – especially in the construction sector – increasing somewhat from the previous survey. Prices remained flat at the retail level and mixed for manufacturing materials, while prices for some construction materials began to rise.

Retail Sales. The momentum created by stronger than expected retail activity during the holiday and post-holiday seasons continued in February, as sales compared with both the previous month and previous year again posted solid gains. At least part of the robust activity was a result of pre-spring clearance sales. Many stores have now begun increasing stock levels again to get ready for the spring season, and further expansions are planned in coming months. With consumers remaining predominantly upbeat about the economy, most retailers expect continued strong sales. Automobile sales remained somewhat slow in February, especially for small passenger cars, leaving sales below year-ago levels. Truck and SUV purchases continued to rise, however, keeping dealers fairly content with current inventory levels. Dealers expect an upturn in overall vehicle sales within the next few months unless credit conditions change considerably.

Manufacturing. Tenth District manufacturing activity improved slightly last month but is still rather weak overall. Nearly all plants were operating at medium to high levels of capacity, which was an improvement over our previous survey but still well below the activity level of last summer. Manufacturing materials remained generally available, with virtually no variation in lead times and no major difficulties expected in the near future. Managers continued to trim inventories as fears of reduced exports and increased imports heightened after the Brazilian currency devaluation in mid-January.

Inventory cutbacks were not as sharp as in the previous survey, but many managers remained unsatisfied with current stock levels and plan to keep trimming over the next few months.

Housing. Construction activity eased slightly last month due to colder weather, but starts were still well above year-ago levels. Home sales also weakened a bit in February, pushing inventories of unsold homes slightly higher. New home purchases continued to outpace last year, however. Builders expect strong expansion of construction activity over the next three months. Mortgage demand remained flat in February, dropping slightly below year-ago levels. Small increases in interest rates may have helped slow both refinancing activity and new home purchases. But mortgage bankers concur with developers that activity will soon pick up and lenders therefore believe that loan demand is likely to grow much faster in the near future.

Banking. Bankers report that loans increased while deposits fell last month, increasing loan-deposit ratios. Demand increased for consumer loans, home equity loans, commercial real estate loans, and agricultural loans. On the deposit side, demand deposits, NOW accounts, and large time deposits all decreased slightly. All respondents left their prime lending rates unchanged, and the majority left consumer lending rates unchanged last month. All banks expect to leave the prime rate unchanged, and most expect to hold consumer lending rates steady in the near term. A few banks reported a tightening of lending standards on agricultural loans because of concerns over low commodity prices.

Energy. District energy activity continued to decline in February, as prices took another turn for the worse. The rig count fell 8 percent, following an even bigger drop in January, to 44 percent below year-ago levels. After rising moderately in January, the price of West Texas Intermediate crude oil fell 2 percent in February, as world demand failed to pick up in the wake of the Brazilian crisis. At $11.96 per barrel, oil was 26 percent cheaper than a year ago. Natural gas prices also fell after recovering slightly in January. Mild weather and a glut of gas on the market led to a 5 percent price decline in February, to 18 percent below the previous year.

Agriculture. The district's winter wheat crop was in good condition, although unusually warm weather led to early development, leaving the crop open to damage from a late freeze. The existing wheat pasture was in good shape. Hog producers in the district continued to struggle due to low market prices and many small and mid-sized producers have liquidated their herds. The remaining producers are expected to hold out another six months for higher prices. District farmland values remained stable, although sales volume was down. Landowners are being more flexible with rent payment schedules, but district cash rents held steady. District bankers indicated that credit reviews of agricultural borrowers look good. In most cases, less than 5 percent of the banks' agricultural loans will not be renewed, about the same percentage as a year ago. However, district ag bankers are requiring more of their customers to obtain federal loan guarantees this year, reflecting some concern about repayment difficulties in the year ahead.

Wages and Prices. Labor markets remained very tight in most of the district last month, with wage pressures – especially in the construction sector – increasing somewhat from the previous survey. Retailers continued to have problems finding entry-level workers and sales associates. Labor shortages among manufacturers were less widespread than in previous surveys, but general laborers were still in need. Builders faced the biggest difficulties obtaining workers, despite a slight easing in the overall construction market. All types of construction workers were in high demand, especially skilled tradesmen such as framers, bricklayers, and carpenters. Builders subsequently felt the biggest increase in wage pressures in February, although retailers were also forced to increase pay more rapidly than in the recent past. Thanks to a reduction in labor tightness among manufacturers, wage pressures in that sector subsided somewhat compared with previous surveys. Retail prices held steady in February and are expected to remain stable in the near future. Prices of manufacturing materials were mixed. Steel prices continued to drop, but rubber and plastic prices both increased. The price of some construction materials, such as insulation and sheetrock, also edged up, and further small increases for some materials such as drywall are expected in the near future.

ELEVENTH DISTRICT--DALLAS

The Eleventh District economy continued to expand in February and early March, with some sectors reporting stronger activity than in the last beige book. Retailers said sales growth was stronger than expected, and some manufacturing sectors reported improved sales. Real estate activity picked up, but there continued to be some concerns about overbuilding, particularly apartments. Business service firms reported little change in activity overall. Most financial institutions reported a strong start to 1999, with the exception of banks lending to the agricultural and energy industries. Drilling activity continued to plunge, reducing demand for energy service and manufacturing firms. Dry conditions remain a concern for agricultural producers, with many farmers and ranchers still in serious financial jeopardy after last summer's drought and low commodity prices.

Prices. There continued to be more reports of price declines than price increases. Finding qualified workers remains a problem for most industries, with many contacts reporting higher wages. Crude oil prices stayed between $11 and $13 over the past six weeks, and there was no indication that the glut of crude and oil products was anywhere near an end. Distressed oil companies are selling existing reserves to reduce debt, and the availability of these low-cost reserves is discouraging drilling. With the end of the heating season approaching, high inventories and continued warm weather pushed down heating oil and natural gas prices. Heating oil prices fell below 30 cents per gallon, but returned to 33 cents per gallon by the end of February as refiners pulled unprofitable capacity off line. Heating oil inventories are 17 percent above last year's levels. Wellhead natural gas prices fell from $1.85 to $1.65 per thousand cubic feet during the month of February. Retailers said selling prices were mostly unchanged, and some contacts expect apparel price reductions in the Spring. A number of maintenance outages led to a drop in ethylene inventories and chemical operators announced price increases, but large capacity increases are scheduled in coming months, so price increases are expected to be short-term at best. Prices have increased slightly for many types of semiconductor chips, but continue to decline for telecommunications equipment.

Manufacturing. Some manufacturing sectors reported improved sales growth, but energy-related and most apparel manufacturers continued to hemorrhage. Conditions in the semiconductor industry continued to improve, with contacts reporting that the outlook for prices and sales improved significantly. World inventory of the consumer products that use chips has dwindled and demand in Asia has begun to recover, according to one source. Another respondent noted that several of the smaller producers of memory chips have left the market, resulting in reduced production. Telecommunications manufacturers reported solid gains in demand and a strong outlook over the next year. Food manufacturers said demand remains good, with no signs of weakening. Metals producers report a pick up in demand. Brick and concrete producers reported continued strong sales, boosted by housing starts, low interest rates and commercial building. Demand for industrial paper products was strong, but demand for boxes was weaker than expected. Demand for lumber products softened over the past month and is lower than a year ago, although contacts expect a modest rebound. Refiners have taken capacity off line, and operating rates have fallen by 4 percent to 5 percent. Apparel manufacturers reported weaker sales and layoffs, mostly because of intense competition from cheaper imports.

Services. Business service firms reported little change in activity overall. Demand for legal services was down from a year ago, in part because of slower demand for transactional work such as real estate services. Contacts reported an increase in trial and litigation work, however, and continued strong demand for legal services related to the high tech industry and intellectual property rights, patents and trademarks. Temporary service firms reported little change in activity over the past month, with strong demand from telecommunications firms, call centers, and banks. Demand for temporary workers for manufacturing and defense was weaker and "pitiful" for oil industry workers. Transportation firms reported that activity was mostly stronger than expected.

Retail Sales. Retailers said sales activity was stronger than expected in February. All types of products were selling well, particularly spring merchandise and home goods, such as appliances and furniture. Retail contacts were in good spirits, noting that consumers appeared to be feeling comfortable. One contact attributed the strength of sales growth to an increase in tax refunds. Auto sales were also up, with good demand for trucks and sports utility vehicles. Inventories are tight for some of these vehicles, in part because inventories are still recovering from the GM strike.

Financial Services. Most financial institutions reported a strong first two months of 1999. Auto lending, home equity refinancing and deposit growth all showed signs of strength, according to bankers. Credit quality and delinquency rates remained stable. The only contacts who were not positive were those with high levels of lending to the energy sector and financial institutions in rural areas, who are seeing trouble with agricultural loans.

Construction and Real Estate. Real estate activity picked up in late February and early March, after a slowdown in January and early February. There continues to be no speculative construction, however. Sales of existing homes were exceptionally strong. Office occupancy rates are expected to fall by 1 to 3 percentage points this year, because contacts expect a high level of office completions and slower office leasing. Office and apartment rent concessions continued to be reported in some markets, and contacts still express concerns about some overbuilding, particularly apartments. Industrial construction was slower but leasing activity was steady.

Energy. Low oil prices, large inventories, and concerns that broader structural changes are afoot, are all contributing to a serious decline in drilling activity. Domestic drilling has fallen 23 of the last 25 weeks, and contacts do not believe the rig count has bottomed out. Demand for energy services has declined with the rig count. Demand for pipe, machinery and equipment has fallen more than the rig count because a lot of rigs are being idled, providing a ready supply of cheap spare parts. Offshore drilling had been holding up well, but contacts say some shallow-water rigs are being taken out of service as well. Unlike oil prices, natural gas prices remain high enough to provide some incentive for drilling.

Agriculture. Many of the region's agricultural producers remain in serious financial jeopardy. Agricultural bankers reported that farmers and ranchers continue to have difficulty repaying loans because of last summer's drought and low commodity prices, and producers continue to leave the business. There is concern about the current lack of moisture, and some farmers have delayed planting while waiting for rain. The lack of rainfall has stressed pastures in many areas, and supplemental feeding has been steady. Growth of small grains was slow, but mild temperatures allowed fields to stay green.

TWELFTH DISTRICT — SAN FRANCISCO

Summary

Reports from contacts indicate strong performance from the Twelfth District economy in recent weeks. Sales of retail merchandise and services were robust in most areas of the District. Responses suggest a slight acceleration in District manufacturing activity, although demand in key sectors continues to be hampered by adverse trade conditions. District agricultural producers were hindered by weak export demand and poor weather. Conditions in real estate markets and the market for bank credit were robust overall, although slower real estate and construction activity was evident in some states. Upward price pressures were limited overall.

Business Sentiment

District respondents were optimistic about the expected performance of the national economy and their respective regional economies during the next four quarters. Virtually all of the respondents expect growth in national GDP to equal or exceed its long-run average pace. Slightly over half expect unemployment and inflation to remain unchanged, although about 40 percent expect these measures to rise. About half of the respondents expect better growth performance in their regions than in the nation as a whole; this percentage is up a bit from last fall. Moreover, the percentage of respondents expecting deterioration in their region's outlook for foreign trade has fallen substantially since last fall, although it remains slightly above one-half.

Retail Trade and Services

Sales of retail merchandise and services were rapid. Unit sales of retail merchandise were high in most areas, with substantial discounting reported; specialty retailers did particularly well.

Sales of new automobiles and light trucks were vigorous, picking up in late February following typically slow seasonal sales in preceding weeks. Respondents in several areas noted strong sales growth at supermarkets. Retail inventories generally were in balance, with the key exception being short supplies of some new trucks and sport utility vehicles. Prices of most products reportedly were steady, with the exception of an increase in the prices of retail pharmaceuticals. Sales of telecommunications services, internet-related services, and computer software were strong. Port traffic was very high on the West Coast, as East Asian imports continued at a rapid pace while export traffic reportedly has stabilized and possibly even picked up a bit.

Manufacturing

District manufacturing activity reportedly picked up a bit recently, although demand in key sectors continues to be hampered by adverse trade conditions. Unit sales of high-tech equipment were solid, reportedly due in part to mild improvement in East Asian exports; this has been accompanied by slower declines in the prices of semiconductors and other computer components. A pickup in production and sales of wood products was reported for the Pacific Northwest. Production activity and sales were very strong for manufacturers of communications equipment, automobiles, and pharmaceuticals. In contrast, Boeing has seen cancellation of aircraft orders from China and other East Asian countries; reduction of the company's workforce has proceeded, and Boeing's suppliers are facing reduced demand due to the company's production cuts. In the machine tool, steel, and garment manufacturing industries, respondents noted stiff competition from low-priced imports, accompanied by shrinking employment in each industry and rising inventories in the latter two.

Agriculture and Resource-related Industries

District agricultural and natural resource suppliers faced somewhat weak conditions. Citrus growers in California's Central Valley suffered severe crop damage due to the freeze in late December. The associated losses were large in dollar terms, which has hurt the area's income, employment, and retail sales performance. Throughout the District, prices remained very low for key agricultural commodities, especially wheat. District beef sold well, due to strong exports to Mexico and a pickup in exports to Japan. In the extraction industries, low prices for oil and natural gas have reduced profits and employment in some areas, most notably Alaska, where oil companies reportedly have cut budgets by 25 to 30 percent.

Real Estate and Construction

Activity in the District real estate and construction sector was robust overall, although slowing was evident in some states. Home construction, sales, and price increases were rapid in most parts of California. A San Francisco respondent reported that lease rates for commercial space in the San Francisco Bay Area rose further, reaching levels equal to the historical highs of the late 1980s. In Hawaii, sales of existing residential properties reportedly were the only source of vigor in the otherwise moribund state economy. In other parts of the District, real estate market and construction activity has slowed a bit, easing earlier capacity pressure. The rate of increase in the cost of housing reportedly has slowed in Idaho, Utah, and Nevada. Respondents also reported that the cost of construction labor has fallen from previously elevated levels in Utah, and construction activity in general fell further in Oregon.

Financial Institutions

Demand for loans was strong in most areas and was met by vigorous competition among banks for loan applicants. Respondents in several areas of the District noted very competitive pricing and underwriting terms for loans. The pace of lending was rapid throughout California, although in the state's Central Valley bank business reportedly was reduced by economic difficulties associated with damage to the area's citrus crop. The only reported instance of deteriorating credit quality was from the Oregon coast, where loan delinquencies increased.